CAP + DIVIDENDS IN DETAIL

THE CAP. Cap + Dividends starts with an economy-wide carbon cap — a limit on the amount of burnable carbon that enters the economy in a given year. The way the cap works is extremely important.

There are two possible places to put a carbon cap: (1) where CO_2 leaves the economy and enters the atmosphere, and (2) where carbon enters the economy in the form of a fossil fuel. Economists call the former a *downstream* cap and the latter an *upstream* cap.

In choosing where to put the cap, it's important to recognize how carbon differs from other pollutants. Most pollutants are minor impurities that can be regulated at the ends of pipes or smokestacks. Carbon, however, is ubiquitous — it gushes not just from a few pipes, but from hundreds of millions. Capping carbon *downstream* is therefore extremely difficult. To the extent it can be done, it will be an administrative nightmare for businesses and government. And it will never catch all the carbon that flows into the atmosphere.

By contrast, capping carbon *upstream,* as it enters the economy, catches all the carbon that ultimately flows into the atmosphere, and is astonishingly easy to administer. Only a few hundred companies bring fossil fuels into our economy; a cap would be administered by requiring these companies to buy permits. The number of permits each company needs would be based on the carbon content of its fuels. Once a year the companies would 'true up' and pay a stiff penalty if they don't own enough permits. No other businesses would need permits, and no smokestacks would need to be monitored.

THE DIVIDENDS. When fuel companies buy permits, they'll pass that cost along to their customers. This is as it should be: the cost of emitting CO_2 *needs* to be paid by energy users. By adding this currently ignored cost, we'll shift private investment away from fossil fuels and toward clean energy.

Higher fuel prices have a downside, however: they take lots of money out of everyone's pockets. The trillion dollar question is, *where does that money go?*

In traditional cap and trade, the extra money we pay goes to companies who get free carbon permits. Under Cap and Dividend, it flows into a trust. It's then divided into equal shares and wired to everyone's bank account or debit card. This happens monthly and automatically. No large bureaucracy is needed.

CAP + DIVIDENDS COMPARED TO CARBON TAXING

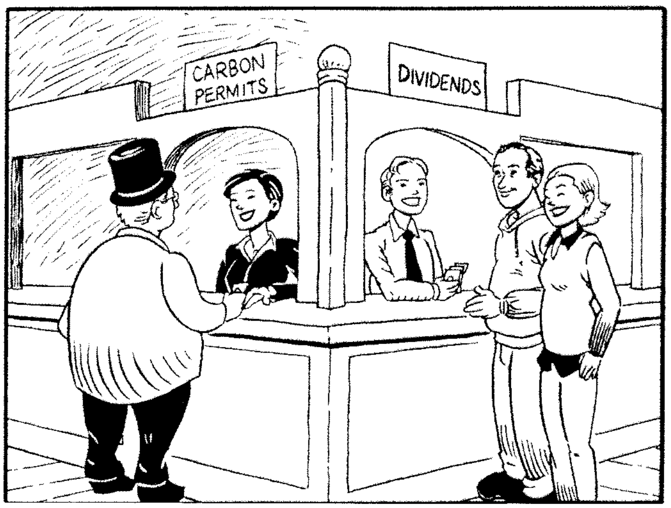
Some economists favor a tax on carbon as an alternative to carbon capping. The revenue raised by such tax would be returned to the economy by cutting other taxes. This is called 'revenue neutrality.'

Proponents of a carbon tax say it's simpler than a cap and less exploitable by special interests. This is true if the cap is *downstream*. But if the cap is *upstream*, those advantages vanish. With an upstream cap, the same companies that would pay a carbon tax would buy permits instead; no other businesses would be involved. Giveaways to special interests would be avoided by selling permits in competitive auctions.

In essence, an upstream cap is like a carbon tax with two differences. One difference is, a cap physically limits pollution. With a tax, the *price* of pollution will rise, but there's no assurance that the *quantity* will decline, or decline fast enough to meet our goal and timetable.

The second difference lies in how revenue is recycled. Some carbon tax proponents favor reducing corporate income taxes. Others would reduce personal income taxes, state sales taxes or federal payroll taxes. In all these cases, *some* Americans would get money back, but millions wouldn't.

The most progressive carbon tax proponents – including Al Gore – favor refunding a portion of payroll taxes. This would benefit roughly 100 million Americans, but leave out retirees, young people, stay-at-home parents, the unemployed, and everyone working in the informal economy. In particular, it would exclude about half of the poorest Americans and a sizeable chunk of the middle class, all of whom would pay higher energy prices but get nothing back.



In Cap and Dividend, a trust sells permits to fuel companies and distributes the proceeds in equal monthly dividends to all Americans.

The advantage of per capita dividends is that they cover everyone equally. No one is favored or excluded. In addition, dividends are wired monthly to help pay bills. Tax refunds, by contrast, are distributed annually.